

MINUTES

MONTANA SENATE 57th LEGISLATURE - SPECIAL SESSION COMMITTEE ON TAXATION

Call to Order: By **CHAIR BOB DEPRATU**, on August 6, 2002 at 9:00 A.M., in Room 152 Capitol.

ROLL CALL

Members Present:

Sen. Bob DePratu, Chair (R)
Sen. Alvin Ellis Jr., Vice Chair (R)
Sen. John C. Bohlinger (R)
Sen. Mack Cole (R)
Sen. Pete Ekegren (R)
Sen. Jon Ellingson (D)
Sen. Bill Glaser (R)
Sen. Dan Harrington (D)
Sen. Emily Stonington (D)

Members Excused: None.

Members Absent: None.

Staff Present: Lee Heiman, Legislative Branch
Deb Thompson, Committee Secretary

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed.

Committee Business Summary:

Hearing(s) & Date(s) Posted: SB 6, SB 11, SB 12, SB 13,
8/5/2002
Executive Action: SB 6 as amended Passed

Hearing Adjourned at 12:03 and Reconvened at 1:15 p.m.

HEARING ON SENATE BILL 6

Sponsor: Senator John Cobb, SD 25, presented the bill. He said the bill would clean up language. He explained what the TANF money would be used for. He discussed affordable housing and the increase in case loads. **Lee Heiman** passed out an amendment.

Proponents' Testimony: Judy Smith with Homeward Bound in Billings had indicated that regulations made it difficult to access the money. \$200 thousand dollars does go toward affordable housing issues. Honoring contracts for non profit developers was important. **{Tape : 1; Side : A; Approx. Time Counter : 0 - 7}**

Opponents' Testimony: None

Questions from Committee Members and Responses: Senator Ellingson asked about the effect of the \$3.4 million dollar transfer on the TANF funds. Ms. Smith replied the caseload increased for those needing affordable housing. She noted this told something about the economy where people moved into welfare programs, which had the opposite effect of poverty reduction.

Senator Cobb pointed out if case loads go up due to cuts by HB 2, a possible increase in this program of \$200 thousand dollars would be needed. Most of this money had already been contracted to run the program. **{Tape : 1; Side : A; Approx. Time Counter : 7 - 10.1}**

Closing by Sponsor: Senator Cobb closed.

HEARING ON SENATE BILL 11

Sponsor: Senator John Cobb, SD 25, presented SB 11. He explained the bill would allow for a handling fee for the paying of child support payments. He described recent court challenges and court opinions. He said the bill would allow the department to charge the fee. The problem was the department was running out of money. The division was broke and needed the support to get through the rest of the year. He described the cuts and compared human services with K-12. The caseloads were high and the money was short. He pointed out the language in the bill said the department "may" collect fees. It could be decided if the money should go to the General Fund but the option would be available. **{Tape : 1; Side : A; Approx. Time Counter : 10.1 - 16.6}**

Proponents' Testimony: None

Opponents' Testimony: Candy M. Jenkins, a Missoula recipient of child support, said the \$7 fee was meant for support for the children. It is not right to charge a fee as it is taken out of the benefits meant for the children.

Informational Witness: Lonnie Olson, representing the Department of Public Health and Human Services, Child Support Enforcement Division, presented written testimony. **EXHIBIT(tas02a01)** He pointed out the difficulties that would be encountered if this bill passed. He said there were 29 thousand cases and warrants equaled \$300 thousand. There would not be the staffing to do individual determinations. The fees would be questioned as to what legal basis there was to collect them. Those not requesting a service would be asked to pay a fee. Those who were not delinquent and were good actors do not deserve the fee.

Representative Michele Lee from Livingston, described the important service that was provided to children. She pointed out there were 10,400 clients who were non-welfare users. **{Tape : 1; Side : B; Approx. Time Counter : 0 - 3}**

Questions from Committee Members and Responses: **Senator Bohlinger** asked how this could be viewed as positive since it affected the number of federal dollars received. **Senator Cobb** replied this would be applied to the division as they were still short money and would need a supplemental if something were not done. He suggested this bill would give them the option to collect the fee and allow them to be pro-active.

Closing by Sponsor: **Senator Cobb** closed.

HEARING ON SENATE BILL 12

Sponsor: **Senator John Bohlinger, SD 12, Billings,** discussed the proposed cuts and the long term policy changes. He noted that concern for the poor did not wear party labels. He pointed out the Governor had ordered \$38 million dollars spending adjustment and the budget now was faced with a \$45 million dollar short fall and further reductions would be necessary. New tax revenue would be important. He pointed out that SB 12 would raise \$40 million dollars annually. He explained the increase of the bed tax from 4% to 9% was still under the national average of 12%. He described comparisons with neighboring states, where Idaho had an 8.33 percent tax, Utah-17.1%, Nevada-16.25%, New Mexico-10.10%, Arizona-9.27%, North Dakota-8%, South Dakota-7.67, Colorado-7.02 and Wyoming-6%. Additionally, other states have a sales tax including meals and other things which provide an effective tax rate of 12%. The Department of Revenue has indicated a 5% increase would give the budget \$15 million dollars a year. Some say tourists won't come - but do you believe it? A 9% car rental tax is less than any of ten states in the region which averages 13.87%. He distributed a table showing rental car tax state by state comparisons. **EXHIBIT(tas02a02)** He said to keep in mind

the national average for a car rental tax was 13.87% and Montana should move closer to the average. He said the final component of his bill would move the tobacco tax to a .42 cent increase which places it near the national average. This would increase the General Fund by \$18 million dollars in 2003 and \$23 million by 2004. This also takes into consideration the reduction of new smokers. He pointed out a transfer of new revenue to the General Fund would help eliminate the need for further reductions. His constituents say let the tourists share in the cost of services. If there were a tax increase on cigarettes the young may quit or never start. These effect health matters of great consequence. This will be reflected in health costs and insurance. Tobacco kills more people annually in Montana where \$216 million dollars are needed to treat tobacco related illnesses. **{Tape : 1; Side : B; Approx. Time Counter : 3 - 24.7}**

Proponents' Testimony: Dr. Robert Shepard, representing the American Cancer Society, described the economic impact of cigarette smoking and the issue of second hand smoke. He said there was a 50 year old study regarding the ill effects. He talked about the smoking ordinance that was recently passed in Helena. **{Tape : 1; Side : B; Approx. Time Counter : 24.7 - 30}**

Dick Crofts, Commissioner of Higher Education, presented written testimony urging the committee to pass this bill. He described the effect of the loss of funding over eleven years and now there were more students attending the universities. **EXHIBIT(tas02a03)**

Erin McGowan, representing Protect Montana Kids.org, said her organization fought death and disease caused by tobacco. She supported SB 12. She talked about the smuggling issue and the fact that most people bought single packs as they were interested in convenience. 70% of smokers wanted to quit.

Cliff Christian, American Heart Association, discussed the tobacco settlement which he felt was for past harm.

Jack Copps, Executive Director of the Montana Qualified Education Coalition, said he felt this bill offered a solution for an increase of revenue. He pointed out Montana paid the 3rd lowest tax in the nation.

Darrell Rud, Executive Director of the School Administrators of Montana, read his written testimony. **EXHIBIT(tas02a04)**

Dave Puyer, Montana Rural Educators Association, discussed the rural school budget shortfalls and the difficulty in retaining teachers. **{Tape : 2; Side : A; Approx. Time Counter : 17.8 - 18}**

Eric Feaver, said he supported SB 12 as a solution for developing a revenue stream. He discussed a questionnaire that had been sent to their members regarding the various tax proposals. {Tape : 2; Side : A; Approx. Time Counter : 18 - 22.9}

Jim Smith, representing the Montana Peace Officers and the County Attorney Association, pointed out the need for adequate funding of public safety, public services and institutions.

Opponents' Testimony: **Jerome Anderson**, representing R.J. Reynolds Tobacco Company, testified against the bill. He presented written testimony. EXHIBIT(tas02a05) EXHIBIT(tas02a06) EXHIBIT(tas02a07) He described his disagreements with statements made by the proponents. He felt the financial obligation was already too great and should not be increased. He stressed that according to the settlement agreement both past and future harm to smokers was addressed. {Tape : 2; Side : A; Approx. Time Counter : 22.9 - 29.4}

Steve Wade, representing Phillip Morris, pointed out that a tax increase should not be considered without first addressing the Internet and mail order situation. He presented an article regarding smuggling. EXHIBIT(tas02a08) He said this tax would negatively impact the revenue to the state where jobs and individuals would be significantly impacted. He felt taxes should be broad based. {Tape : 2; Side : B; Approx. Time Counter : 0 - 3.4}

Kurt Alme, Director of Department of Revenue, asked the committee not to support SB 12. He stressed that the Governor did not support any tax increases. {Tape : 2; Side : B; Approx. Time Counter : 3.4 - 4.5}

Amy Sullivan, Montana Tourism Coalition, said their group did not support this. She pointed out the economy was down with the number of travelers soft. People had changed their travel plans and were staying in more campgrounds. It was not a good time to look at tourist statistics since there was a loss in the tourism sector of 28 thousand jobs.

Ken Nordvedt from Bozeman, said there was no evidence that tourists did not pay for services. He said the real goal was to cut government spending. {Tape : 2; Side : B; Approx. Time Counter : 4.5 - 9.9}

Candace Payne, representing the Montana Car Rental Association, opposed the bill. She suggested tax reform was needed.

Jeff Taylor, representing Rent-A-Wreck in Missoula, said his business was an off-airport rental company and they were still assessed a fee by the airport for access. He noted this was unfair for one industry to be taxed. Most of their business was in local residents, not tourists as was suggested. **{Tape : 2; Side : B; Approx. Time Counter : 9.9 - 13.4}**

Rob Doyle, Avis Rent-A-Car from Missoula, Kalispell and Billings, said the tax was selective and would put their business at a disadvantage.

Jerry Woodahl, a rental business in Missoula, said a tax should be broad based. He pointed out the rental car business paid \$45 thousand dollars in vehicle license fees to public schools. The \$200 thousand dollars paid to the airports in Missoula was paid by the rental car businesses, not the county. **{Tape : 2; Side : B; Approx. Time Counter : 13.4 - 15.5}**

Mark Staples, Montana Wholesale Distributors, described his opposition to a tax increase. He pointed out the wholesalers would be "whacked" twice by paying for a tax increase plus an inventory tax. Smuggling was on the rise over the Internet and mail. Teachers were underpaid and education was underfunded. **{Tape : 2; Side : B; Approx. Time Counter : 15.5 - 18.9}**

Steve Turkowicz, representing the Auto Dealers' Association, did not feel this tax was the way to go. Montana's ranking was 48th in the nation with a comprehensive tax.

Tim Peiper, representing Hertz Rent-A-Car in Helena, opposed the bill.

Robert Ward, Enterprise of Montana in Helena, opposed the bill.

Lara Kline of Hertz of Great Falls, opposed the bill.

Stuart Doggett, Montana Innkeepers Association, opposed the bill.

Bob Pavlovich of Butte, opposed the bill. He pointed out a balanced budget should be fair. He suggested a one cent tax on toilet paper.

Webb Brown, Montana Chamber of Commerce, opposed the bill.

Spook Stang, Executive Vice President of the Montana Motor Carriers' Association, opposed section six in the rental vehicle surcharge of one ton or less.

Steve Costley, representing the Car Rental Association, was against the bill.

Informational Witness: **Chris Gallus, an attorney from Butte,** spoke about the smoking ordinance. He said there was rumors regarding trade-offs with the tobacco tax. He said there was no conspiracy or deals made. **{Tape : 2; Side : B; Approx. Time Counter : 18.9 - 25.8}**

Questions from Committee Members and Responses: **Senator Harrington asked Amy Sullivan** why their industry felt the tourist tax was their money? He pointed out the Legislature had the right to cut or raise the tax. **Sullivan** pointed out this money had been set aside for tourism promotion.

Senator Ellingson asked Kurt Alme about the executive branch lack of support for a tax increase during the Special Session and were there any plans to address tax reform. **Alme** replied they were working on a plan. **{Tape : 3; Side : A; Approx. Time Counter : 0 - 3.8}** He noted they were looking at the local options tax idea, reappraisal was coming at the end of the year and they would be looking at the property tax system. **Senator Ellingson** asked why they did not look at new taxes so there was time for public discussion. **Alme** pointed out with the shortfall they were facing, it was not appropriate to look at a tax increase.

Senator Harrington pointed out the health care, education and corrections made up 70-80% of the budget. He noted with a \$250 million dollar shortfall in the coming months, how could the administration consider \$31 million dollars of additional tax cuts in view of this structural imbalance. **Alme** replied that the Governor and the advisory council that considered these issues regarded a higher income tax or capital gains tax as an impediment to economic development. He said it was not appropriate to backfill revenue losses with taxes. **{Tape : 3; Side : A; Approx. Time Counter : 3.8 - 9.5}**

Closing by Sponsor: **Senator Bohlinger** closed. He commented that he had been a member of the tax committee for three terms and the committee had been benevolent by giving money away. He pointed out they had lowered the business equipment tax which he supported but the committee must raise taxes as new revenue was needed. He urged the committee pass SB 12 to bring the bill to the full Senate body. **{Tape : 3; Side : A; Approx. Time Counter : 12.4 - 15.8}**

The Committee adjourned at 12:03 and reconvened at 1:15.

HEARING ON SENATE BILL 13

Sponsor: Senator Dan Harrington, SD 19 in Butte, presented the bill. He said the bill would clarify the intangible property tax so software, if purchased, could stay within the tax system. He pointed out there was a one million dollar hit on the property tax collections in Butte if clarification fails. The local government in Butte would need to repay the Department of Revenue.

Proponents' Testimony: Alec Hansen, League of Cities and Towns, described the revenue loss from this situation. He asked if the state was obligated for refunds if it was determined that the software could be depreciated. He asked why the software in Butte was taxed last year and now was exempt. He said this needed clarification.

Pam Haxby Cote, Community Development Director of the city of Butte, stressed the funding error meant \$1.3 million dollars to Butte Silver Bow. She asked about commercially developed software and whether it was exempt. She noted that some of this software was valued at \$20 million dollars. She asked about the statewide effect on other counties. *{Tape : 3; Side : A; Approx. Time Counter : 15.8 - 27.7}*

Judy Jacobsen, Chief Executive of the city of Butte, said she believed it was the intent of the legislature to exempt in-house developed software. She pointed out the ramifications of not clarifying this law could effect the whole state. The dilemma means Butte could loose \$1.3 million dollars.

Senator Debbie Shay, SD 18 in Butte, said the bill addressed a serious problem in each community. She pointed out a million dollar hit in any community was devastating. *{Tape : 3; Side : B; Approx. Time Counter : 0 - 1.6}*

Opponents' Testimony: Mary Whittinghill, Montana Taxpayers' Association, discussed the different treatment of intangible property. She talked about mineral rights and even telecommunications which could be considered intangible. She pointed out that Washington, California, Texas and Idaho do make specific exemptions for those that centrally assess or those with intangible property. She said that there should be a determination regarding the differences between custom built software and commercially purchased which can be depreciated and would not be considered intangible. She talked about the effect of taxing a high tech company on something that was never taxed before. She said it would be difficult to determine market value

on licensed software that was not owned and could not be sold.

{Tape : 3; Side : B; Approx. Time Counter : 1.6 - 8.2}

Webb Brown, representing Montana Chamber of Commerce, opposed the bill.

Jeff Elers, Montana Telecommunications Association, said his association opposed a software tax. He pointed out the need for predictability in regards to staffing, business plans and that budgets are already set. He pointed out the difficulty in changing the laws every two years. **{Tape : 3; Side : B; Approx. Time Counter : 8.2 - 10.9}**

Questions from Committee Members and Responses: Senator

Stonington asked **Gene Walborn** from the Department of Revenue to clarify the history of software purchases whether it was taxed one year and not the next. **Walborn** said he would have to look to see it was reported on the personal property forms. **Senator Stonington** asked about the differences between property that was centrally assessed or was intangible property. **Walborn** replied that Department of Revenue developed rules regarding the value of centrally assessed property, referencing SB 111. He noted multi-state companies had to be considered. He said breaking out and valuing intangible property was a problem. Electric companies have at least 10% of their value that is exempted as it can be demonstrated that the value is associated with intangible personal property. He noted software was not valued separately but as intangible personal property as a whole. Northwestern energy was exempted last year from this market value by using a default percentage but if it was reported on their personal property form they would have been taxed. **{Tape : 3; Side : B; Approx. Time Counter : 10.9 - 16.6}**

Senator Stonington asked how the error had been found in Butte. **Pam Cote** talked about the budget preparation and the software issue. She said it was acceptable accounting principles that intangibles are not taxed such as licenses, internally created software or trademarks. Commercially purchased software is different and is treated like an asset and should be taxed. A distinction needs to be made. She noted that Butte had \$22 million dollars of commercially purchased software.

Senator Bohlinger asked **Gene Walborn** how software that was leased was treated differently. **Walborn** said there were three ways to treat the software. One, it could be treated as an expense - such as Turbo Tax. Two, it could be depreciated if it comes with hardware and the value cannot be broken out with just the software. Three - it depends on the life of the product whether it can be capitalized and depreciated. The county leases the

hardware and so meets the test to be able to depreciate. **Senator Bohlinger** asked how the law would affect the tax consequences when applied to the Butte situation. **Walborn** said it should have the same application.

Senator Glaser pointed out the taxes interrelate and the Butte situation is a sizable amount of money. He requested a report regarding what this would mean overall to the state. *{Tape : 4; Side : A; Approx. Time Counter : 0 - 1.4}*

Walborn pointed out the parameters were set by the IRS Code of what can or cannot be an expense, capitalized or depreciated. There are two types of bases - those that are operational or those that are leased. Software has a ten year base. **Senator Ekegren** pointed out the software can be obsolete in ten years. **Walborn** said regardless of whether it is obsolete or not it is still depreciated within ten years. The guidelines have been established. *{Tape : 4; Side : A; Approx. Time Counter : 7.8 - 9.4}*

Senator Ekegren asked how the whole state was affected. **Walborn** said it did impact every jurisdiction, including companies such as Burlington Northern/Sante-Fe. He said it was a fact that intangibles had a certain amount of market value. **Alme** clarified that the first issue was the question of whether software could be exempted as an intangible asset. He pointed out the asset list given by Northwestern had been allocated and spread over the whole state. He said there were two issues: one - is software an intangible and two, what is the impact to the state.

Senator Ekegren asked about the \$1.3 million dollar shortfall to Butte. **Cote** replied that the records indicated they would take a hit but this could effect every county in the state that purchases software. She asked what effect this would have on other counties that were centrally assessed or had all intangibles. **Alme** replied it would be an impact to the state if it was a mistake. It was important to narrow the definition of what was intangible. **Senator DePratu** said that any information as to impact that would help reach a decision would be appreciated. **Senator Cole** said he would need examples of how this impacted local governments. **Senator Stonington** pointed out that now that the issue was brought up, there was a need to focus on rules and the process of defining how business assets are depreciated. *{Tape : 4; Side : A; Approx. Time Counter : 9.4 - 26.2}*

Closing by Sponsor: **Senator Harrington** closed. He talked about how the school equalization issue had an impact on centrally

assessed property. He noted the importance of discerning which types of software were intangible. Local governments were not ready for more tax cuts as it would effect school districts.

{Tape : 4; Side : A; Approx. Time Counter : 26.2 - 29}

EXECUTIVE ACTION ON SENATE BILL 6

Senator Ellis moved do pass SB 6. He moved the amendment. The question was called on the amendment. The motion passed unanimously, with Senator Ekegren absent.

Senator Harrington moved do pass as amended. The question was called. The motion passed unanimously, with Senator Ekegren absent. ***{Tape : 4; Side : B; Approx. Time Counter : 0 - 2.1}***

ADJOURNMENT

Adjournment: 2:02 P.M.

SEN. BOB DEPRATU, Chair

DEB THOMPSON, Secretary

BD/DT

EXHIBIT(tas02aad)